Moody's Investors Service

New Issue: **MOODY'S ASSIGNS MIG 1 RATING TO $27 MILLION MAINE G.O BOND ANTICIPATION NOTES**

Global Credit Research - 25 Jan 2010

APPROXIMATELY $530 MILLION OUTSTANDING G.O. BONDS RATED Aa3 WITH STABLE OUTLOOK

State
ME

Moody's Rating

ISSUE	RATING
General Obligation Bond Anticipation Notes	MIG 1

Sale Amount	$27,000,000
Expected Sale Date	01/26/10
Rating Description	General Obligation Bond Anticipation Notes

Opinion

NEW YORK, Jan 25, 2010 -- Moody's Investors Service has assigned a MIG 1 rating to the State of Maine's $27 million General Obligation Bond Anticipation Notes. Assignment of our highest quality short-term rating reflects the state's financial strength and well-established record of market access. Maine plans to sell the bond anticipation notes the week of January 25. The state's capital program regularly utilizes bond anticipation notes for interim financing, and the state has authorized long-term bond issuance for the various capital projects financed with these notes. The state plans to permanently finance the notes with proceeds from long-term bonds prior to note maturity on June 15, 2010.

Maine's long-term general obligation bonds are rated Aa3 with a stable outlook. Maine's financial operations are narrow, with slim cash balances and rainy day funds depleted at the end of fiscal year 2009. Revenue underperformance due to the recession challenged the state to resolve a $129 million gap in the 2008-2009 biennial budget and a $440 million shortfall for the 2010-2011 biennium. A budget gap of similar magnitude ($438 million) was identified in the state's revenue forecast revision in November 2009, and the Maine legislature is in the process of considering the governor's proposed plan to eliminate the latest shortfall. Liquidity remains tight although Maine has used interfund transfers to avoid short-term borrowing for cash flow in the past several years. The state is authorized to sell $150 million in cash flow notes for fiscal year 2010 but has not yet announced issuance plans. Maine's overall management strength is underscored by efforts to rebuild reserves following the last recession and to control costs while stepping up state spending on K-12 education as mandated by a citizens' initiative approved in 2004. While Maine continues to lose jobs, the overall pace of employment decline is slightly less than the nation.

Long-term credit strengths of the state:

*Management of spending levels while absorbing substantial K-12 education costs mandated by citizens' initiative approved in 2004

*Commitment to improving available reserve levels to enhance financial flexibility

*Alternative liquidity in treasurer's cash pool eases concerns over very narrow General Fund ending cash balances

*Below average debt ratios (per capita and personal income) and rapid 10-year retirement of principal (general obligation bonds) provide flexibility to shift from pay-go to debt capital financing

Long-term credit challenges for the state:

*Weak GAAP-basis balance sheet reflecting negative position of state's General Fund unreserved, undesignated balance

*Depletion of Maine's Budget Stabilization Fund (BSF) to resolve budget gaps leaves state with fewer options to resolve unexpected shortfalls

*Liquidity remains narrow due to negative available combined reserve levels.

*Voter initiative activity adds a periodic element of fiscal uncertainty

*Maine's economic recovery expected to lag the national pace and weak employment prospects hinder Maine's revenue performance

STATE CHALLENGED TO ADDRESS ANOTHER SIZEABLE SHORTFALL FOR CURRENT 2010-2011 BIENNIUM

Maine's revenues have been hurt by the national economic downturn, as they have been in nearly every other state. Moody's assigned a negative outlook to the U.S. state sector in February 2008 and affirmed that negative outlook in February 2009. In the spring of 2009, Maine addressed a fiscal year 2009 budget gap of $129 million as well as a $440 million shortfall for the current 2010-2011 biennium. Now Maine faces another sizeable shortfall of $438 million identified in its November 2009 consensus revenue forecasting process. The gap, which represents a substantial 8% of estimated, and now lower, General Fund biennial revenues, is due largely to revenue underperformance ($383 million). The remaining shortfall is due to $25 million carried forward from fiscal 2009 and $30 million in additional spending pressure, primarily for social services.

The legislature is now considering the governor's proposed plan to eliminate the latest budget gap. Ongoing savings would be achieved through spending reductions in most agencies. The largest cuts would be in human services ($100 million), K-12 education ($73 million), municipal revenue sharing ($27 million), and higher education ($16 million). The state would also add an additional three shut down days. A hiring freeze combined with reorganizations of agencies is estimated to save about $41 million. Excess reserves in the state's retiree health savings would add approximately $70 million in one-time resources, expected to be used in fiscal 2010.

STATE CLOSED $569 MILLION COMBINED BUDGET GAP FOR FISCAL 2009 AND CURRENT 2010-2011 BIENNIUM

Maine relied heavily on one-time measures to close its fiscal 2009 gap, depleting the state's budget stabilization (BSF) and working capital funds, and also using federal fiscal stimulus money, including stabilization and additional Medicaid (FMAP) funds. The state took steps to rebuild its BSF following the last recession, although reserves peaked at a relatively modest level of 4% of General Fund revenues at the end of fiscal year 2008. While Maine has a funding mechanism to refill its BSF from surplus money at fiscal yearend, the state's financial operations will likely remain tight over the next two years, with little margin for rebuilding the BSF in the near term.

The state's gap solution for the originally enacted budget also incorporated approximately $97 million in additional federal stimulus funds through fiscal 2011. Spending reductions accounted for the remaining portion of the gap-closing plan, including cuts to higher education, social services, and elsewhere in state government. Ten state government shutdown days are scheduled for each year of the biennium, and state employees will be required to pay a portion of their health insurance. Federal stabilization money will help the state fund K-12 education at $1 billion in fiscal 2010, up from $983 million in fiscal 2009. This allows school districts time to plan for reduced state education funding ($947 million) in fiscal 2011.

General Fund spending was budgeted at $5.8 billion for the 2010-2011 biennium, the same level as in the 2006-2007 biennium, underscoring the strength of the state's management to reduce spending in the face of reduced resources. As in many states, Maine's federal stimulus funds are being used to fill budget gaps that are due to the current recession. The state's ability to plan for the eventual falloff in additional federal money and restore structural budget balance will be an important credit consideration.

STATE AVOIDED CASH FLOW BORROWING IN LAST THREE FISCAL YEARS BUT MAY STILL ISSUE IN FISCAL 2010; BALANCE SHEET REMAINS WEAK

Maine's year-end cash position remains slim, although fiscal year 2009 marked the third consecutive year that the state was able to avoid the issuance of tax anticipation notes for cash flow purposes. Prior to the recession, the state was able to improve its overall liquidity trends through concerted efforts to hold down expenditure growth, aided by conservative revenue forecasts. Given the recent revenue deterioration and depletion of rainy day funds, Maine may return to cash flow borrowing in fiscal 2010.

Maine's originally adopted budget for the fiscal 2008-2009 biennium closed a structural gap of $570 million, continuing a downward trend from the $733 million gap the state faced in the fiscal 2006-2007 biennium and $1.2 billion prior to that. The state has balanced its budgets in recent years, including the 2008-2009 budget, largely by controlling expenditure growth. At the same time, Maine increased its spending for K-12 education pursuant to a citizens' initiative that requires an increase in state public education funding from its prior level of 49% to 55%, thus providing some property tax relief at the local level. In light of the state's current fiscal challenges, the legislature approved a delay in achieving the 55% state education funding level until the 2012-2013 biennium.

Audited results show that Maine ended fiscal year 2009 with an operating deficit of $35 million. The BSF was depleted, as expected, and the unreserved undesignated general fund balance (UUFB) was a negative $390 million, largely due to several accounting changes in recent years as well as recognition of the state's share of Medicaid liabilities at fiscal year end. However, the UUFB was less negative than the prior year (-$533 million). The state benefited from the increased Medicaid match rate in the federal stimulus plan and was able to address some of the backlog of hospital payments and reduce its Medicaid liability. Still, Maine's balance sheet remains relatively weak with sizeable GAAP negative year-end combined available balances (UUFB plus BSF) recorded since fiscal 2002. Maine's GAAP-basis balance sheet will likely remain weak relative to more highly rated states, reflecting the state's earlier multi-year period of structural budget imbalance, draws on reserves to address revenue shortfalls, continuing education and Medicaid cost pressures, and the continuing revenue shortfalls that increase the state's out-year budget gaps.

VOTER INITIATIVE ACTIVITY CONTRIBUTES TO ENVIRONMENT OF FISCAL UNCERTAINTY

Over the recent past, Maine has faced increased fiscal uncertainty associated with voter initiative activity. Under the state constitution, voters may use the powers of initiative and referendum to initiate legislation in order to change existing statutes, although the constitution may not be amended by this process. Any initiatives or referenda approved by a majority of voters may only be amended or repealed by a majority vote of each house of the state legislature.

A taxpayer bill of rights (TABOR) initiative was rejected by voters in November 2006. In November 2009, voters rejected TABOR II, an initiative that sought to limit increases in state government spending to population growth over the past three years plus inflation in the previous year. As with the first TABOR initiative, TABOR II would have required voter approval of revenue increases and expenditures above the growth limit. Adoption of the TABOR II initiative would likely have added challenges to Maine's budget process, particularly in terms of reduced revenue-raising flexibility. It would also limit the state's ability to build meaningful reserves given reduced incentive to budget expenditures conservatively in order to build up reserves. Maine's success in holding spending growth following the 2001 recession enabled the state to rebuild reserves that provided additional financial flexibility to address the current recession.

MAINE'S ECONOMIC GROWTH SLOWS IN LINE WITH THE NATION

Maine emerged relatively early from the 2001 recession, recovering all of the jobs lost by mid-2004. Between 2004 and 2007, the state's labor statistics maintained some upward momentum but lagged the national pace of job growth. Like that of the nation, Maine's total non-farm monthly employment was essentially flat year-over-year in 2008. The state's education and health service sector continues to gain jobs, although at a slower pace, and to some extent these have helped offset further declines in the state's other employment sectors, especially manufacturing. Maine's paper and textile goods manufacturing sector has been hurt by worldwide competition in those industries. In light of the national recession, prospects for Maine's economy appear modest over the near term, as is true for many states. As the recovery takes hold, Maine is expected to recover jobs at a pace slightly below the national level. Maine's unemployment rate was 8% in November 2009, slightly below its previous peak of 8.6 % in August 2009 and still comfortably below the national rate of 10% in November.

MANAGEABLE DEBT RATIOS; RAPID PAYOUT; NO EXPOSURE TO VARIABLE RATE DEBT OR DERIVATIVES

Maine continues its conservative approach to debt, with an aggressive payout structure and capacity to accommodate unforeseen borrowing needs. Below-average debt levels are in part due to the state's general practice of using available cash rather than new debt to fund approximately 50% of annual capital expenditures, providing additional flexibility to shift to borrowing during periods of economic stress leading to revenue underperformance. General obligation debt amortization is scheduled for a rapid but still affordable 10-year payout, shorter than in most other states. Maine has no exposure to variable rate debt or swaps.

At the end of calendar year 2008, Maine had approximately $978 million in outstanding net tax-supported debt, all fixed rate, and gross debt equaled about $5.1 billion, reflecting a large amount of debt supported by a state moral obligation pledge. Maine's debt ratios for 2009, based on 2008 debt levels, were below average as they have been for the past ten years. The state's net tax-supported debt was 2.2% of total state personal income, lower than Moody's 2009 50-state debt median of 2.5%. Net tax-supported debt equaled $743 per capita, also below our 2008 state debt median of $865.

Maine's total fixed costs, including pension as well as debt service requirements were approximately 10% of operating expenditures in fiscal year 2009. In fiscal years 2002 through 2006, the state made additional contributions above the annual required contribution. These, in combination with improved market results, raised the state's funding levels to 74% as of June 30, 2008. As in many states, significant losses in the equity markets due to the recent market turmoil will be reflected in reduced pension funding levels over the near term although Maine's ratios are somewhat below average to begin with. As of June 30, 2009 Maine's pension funding ratio was approximately 68%. The full annual required contribution for pensions is reflected in the adopted 2010-2011 budget.

Maine pays varying portions of post-retirement health insurance and premium costs for retired employees, depending on the date of retirement, length of service, and Medicare eligibility. The state's most recent OPEB analysis shows an unfunded actuarial accrued liability of approximately $1.2 billion as of January 2009. At the end of fiscal year 2007, the state deposited $100 million into a trust for the OPEB obligation, resulting in a lower overall liability. The annual required contribution was $157 million in fiscal year 2008 and the state contributed $184 million. The state plans to fund its OPEB obligations on a pay-go basis for now.

MOST RECENT RATING ACTION AND PRINCIPAL METHODOLOGY

The last rating action with respect to the State of Maine was on October 2, 2009 when the rating of Aa3 with a stable outlook was assigned to the State of Maine General Obligation Bonds 2009.

The principal methodology used in rating the Maine General Obligation Bond Anticipation Notes was Moody's Methodology Update: Revision to Temporary Criteria for Bond Anticipation Note Ratings published in April 2009 and available on www.moodys.com in the Rating Methodologies sub-directory under the Research & Ratings tab. Other methodologies and factors that may have been considered in the process of rating this issuer can also be found in the Rating Methodologies sub-directory on Moody's website.

Analysts

Nicole Johnson
Analyst
Public Finance Group
Moody's Investors Service

Nicholas Samuels
Backup Analyst
Public Finance Group
Moody's Investors Service

Contacts

Journalists: (212) 553-0376
Research Clients: (212) 553-1653

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